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# DEVELOPMENT EFFECTS OF THE EAST AFRICAN COMMON MARKET

BY

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This paper is really a number of excerpts from a much more detailed and soon forthcoming work on inter-country trade and development policies in East Africa. Consequently, in this paper a number of points are made without discussing them in detail, which would otherwise be necessary.

## I.

As is now well appreciated, the East African customs union has developed into a de facto common market. The East African customs union was formed through four main stages: in 1917 Kenya and Uganda agreed to have free trade in domestically produced goods and to amalgamate their customs authorities; in 1923 Tanganyika, although retaining a separate customs department, was brought into the arrangement; in 1927 free transfer of foreign imported goods was also accepted; and in 1949 Tanganyika's customs department was amalgamated with that of Kenya and Uganda.[1] Besides having free trade in both domestically produced and imported goods, there have been very few restrictions on movements of labour within East Africa. Capital movements have also been free. The result is that a common market has developed, strongly aided by the fact that three countries have common boundaries, share the same currency, and operate a number of services (especially the Railways and harbours, post and telecommunications, the income tax department, and customs and excise department) as joint enterprises under the East African Common Services Organisation (EACSO). In many ways therefore this economic integration is much closer than the one so far achieved by the E.E.C. countries.

In the established theory, economists have tended to discuss the effects of a customs union under the theoretical framework, set up by Jacob Viner, of trade creation and trade diversion effects of such a union.[2] If strictly limited to just assessing trade creation and trade diversion effects, such an analysis is static and would in most cases lead to the conclusion that if most underdeveloped countries formed a customs union they would derive little benefit from it. This is not true, and if such a conclusion emerged, especially in the present world setting, we have good reason to question our theory, or at any rate the premises on which it rests. Rather, what needs to be done is to examine the dynamic effects of such economic integration: we need to examine the effects of the larger market on the growth of output of the whole area; the possible economies of scale and consequent reductions in costs; the possible

1. For a good discussion on the historical development of this customs union see T.A. Kennedy, The East African Customs Union: Some Features of its History and Operation, Makerere Journal, No.4, 1959

2. See Jacob Viner, The Customs Union Issue, New York, 1950

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diversification of the economic activities of the area as a whole (and therefore possible improvements in its terms of trade); the effect on efficiency and productivity through competition; and the effect of such economic integration on inflow of capital and changes in entrepreneurs' outlook. It is also important to examine the effect of the economic integration on the development of each participating country, for what might be true of the area as a whole need not be true of each country.

In this paper we do not have the time to go into all these aspects in detail; instead we shall limit our discussion to (a) the effect of the East African common market on the industrialisation of the area as a whole; (b) the effect of the common market on the development and industrialisation of each country; and (c) possible measures to maintain and improve the working of the common market - for it is now under serious strains and tensions.

## II.

## The Effect of the Common Market on the Industrialisation of East Africa

One of the most serious limiting factors in the industrialisation process of underdeveloped countries is the small size of their domestic markets, for modern mass production of manufactured goods relies, to a very large extent, on large and stable markets. Moverover, the possibilities of underdeveloped countries exporting manufactured goods to the developed countries are very bleak indeed - because such manufactures are produced on small-scale and therefore at high cost; they are initially produced by inexperienced industrialists who have little knowledge of market patterns abroad and who cannot afford to conduct extensive and prolonged advertising campaigns or guarantee availability of spare parts; and, in any case, because the developed countries levy stiff tariffs on manufactured goods coming from underdeveloped countries, with the rate of duty rising, in most cases, with the degree of sophisitication involved in manufacturing e.g. processed primary products are taxed more than unprocessed ones. Furthermore, developed countries can, if imports from underdeveloped countries rise substantially, impose the 'market disruption clause' -- a clause which is not well defined and which could only make sense if the production conditions in the exporting country were truly abnormal, the products were sold at prices very much lower than those prevailing in the market generally, and if further imports of such goods had serious repurcussions in the importing country.[3]

Therefore, the size of the domestic market is of crucial importance in the industrialisation of underdeveloped countries. For any country, the size of the domestic market depends on two factors essentially: the country's population size, and the level of income per head of this population. The latter factor is now the more important one, but it is still true that the smaller the country's population the more permanent will be the constraint of small domestic market on its industrialisation and development. However, although per capita income level is the more important factor, the size of the population, at any given level of income, is of some considerable importance: and economic integration in underdeveloped countries will initally affect this factor, and will be followed, given other factors, by a rise in per capita income. But we need to observe that mere establishment of a common market or customs union among underdeveloped countries, while necessary in most cases,

3. For a more detailed discussion on these factors see my paper, Preferential Trade Arrangements Among Developing Countries, Economic Development Research Project, E.A.I.S.R.

is not a sufficient condition in securing industrialisation: the possibilities offered by such economic integration have to be exploited, initially through establishment and protection of domestic industries designed to produce substitutes for foreign imports.

A good way of assessing the effect of the common market on the industrialisation of East Africa is to examine the growth of trade among the three countries (hereafter referred to as inter-country trade) and its commodity composition. In Table 1a we show the value of East African exports to herself (i.e. inter-country exports), exports to the Neighbours,[4] and exports to the rest of the world - for 1954 and 1959 through 1963. In Table 1 b we show these same exports as percentage shares of total East African exports. In Table 2 we show the commodity composition, by Standard International Trade Classification (SITC) sections, of East African inter-country exports, exports to the Neighbours, and exports to the rest of the world for 1959 and 1963.[5]

From Table 1a it will be observed that while inter-country exports have been increasing steadily, East African domestic exports to the Neighbours and to the rest of the world have been fluctuating and tended to stagnate until 1963. This is reflected in Table 1 b: here we notice that while the percentage share of intercountry exports in total East African exports was only 12.9% in 1954, by 1963 it had risen to 16.5%, and in value terms increased by more than two-and-half times. The fall in the percentage share of these exports in 1963 (it was 17.4% in 1962)was not, of course, due to a fall in the real value: in fact their value increased by £4.7 million. This fall was due to the tremendous increase in the value of East African exports to the other two markets, especially the rest of the world.[6]

The growth of inter-country trade has been of importance in the development of East Africa. Inter-country exports have increased from being less than 4% of these countries' total monetary gross domestic product (GDP) in 1954 to nearly 7% in 1963. This is very important because underdeveloped countries are dependent, and therefore vulnerable, economies because they depend on foreign markets and demand for the disposal of the goods which they produce. Consequently, when demand conditions change in foreign markets, underdeveloped countries are affected directly. Growth of inter-country trade has therefore to be appreciated and stepped up, because it is a movement away from this dependence and introduces a stabilising factor in the development of East Africa.

But perhaps more important has been the rapid increase of manufactured goods in inter-country trade, for this reveals the process of industrialisation which has been and is taking place in East Africa.

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4. For the purposes of this paper the Neighbours are taken to be Zanzibar, Somalia, Ethiopia, Sudan, Congo (Leo.), Rwanda, Burundi, Zambia Malawi, Rhodesia, Mozambique, Madagascar, Mauritius, Reunion & Seychelles.

My study on inter-country trade was substantially completed before Zanzibar joined Tanganyika to form the Republic of Tanzania. Thus in this paper and in my study Zanzibar is not regarded as part of Tanganyika.

5. In both Tables all data on exports refer to goods produced or manufactured domestically i.e. in the case of inter-country exports we exclude transfers of foreign imported goods from one East African country to another; and in the case of exports to the Neighbours and the rest of the world we have excluded re-exports.

6. A large part of the tremendous increase in the value of East African exports to the rest of the world was due to increases in the export earnings of sisal (£10.2mn), cotton £9.4 mn), and coffee (£7.7 mn). These increases resulted from greater quantities of exports, and a minor recovery in the prices of robusta coffee (the prices of arabica and coffee actually declined further). However, the outlook for these commodities is not bright, in view of the world disequilibrium between their supply and demand.

TABLE 1a

EAST AFRICAN INTER-COUNTRY EXPORTS (A), EXPORTS TO THE NEIGHBOURS (B), AND EXPORTS TO THE REST OF THE WORLD (C); 1954, AND 1959-1963

in £ millin.

| | A | B | C |
|---|---|---|---|
| 1954 | 12.51* | 4.08 | 93.00 |
| 1959 | 20.10 | 4.02 | 116.66 |
| 1960. | 22.79 | 4.80 | 126.83 |
| 1961 | 25.04 | 4.55 | 118.71 |
| 1962 | 26.77 | 4.93 | 121.86 |
| 1963 | 31.46 | 5.55 | 153.31 |

* In this figure we have estimated and removed excise taxes on beer, sugar, tobacco, and cigarettes.

TABLE 1b

PERCENTAGE SHARES OF EAST AFRICAN EXPORTS TO A, B & C: 1954, 1959,1962 & 63

| | 1954 | 1959 | 1962 | 1963 |
|---|---|---|---|---|
| All Exports | 100.0 | 100.0 | 100.0 | 100.0 |
| A | 12.9 | 14.3 | 17.4 | 16.5 |
| B | 3.7 | 2.8 | 3.2 | 2.9 |
| C | 83.4 | 82.9 | 79.4 | 80.6 |

Source: Annual Trade Reports of Kenya, Uganda and Tanganyika.

Note: In both tables the figures refer to exports of domestically produced or manufactured goods i.e. in A we have excluded transfers of imported goods, and in B & C we have excluded re-exports

TABLE 2

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COMMODITY COMPOSITION OF EAST AFRICAN EXPORTS TO VARIOUS MARKETS: %SITC* DISTRIBUTION 1959 AND 1963

A = Inter-country exports.
B = Exports to Neighbours.
C = Exports to the rest of the world.

| | 1959 | | | 1963 | | |
|---|---|---|---|---|---|---|
| | A | B | C | A | B | C |
| Value- £ mn | 20.1 | 4.0 | 116.7 | 31.5 | 5.5 | 153.3 |
| SITC Sections | | | | | | |
| 0 | 30.8 | 58.9 | 43.8 | 28.3 | 62.6 | 44.6 |
| 1 | 23.5 | 1.0 | - | 14.5 | 0.9 | - |
| 2 | 3.6 | 15.6 | 45.0 | 2.9 | 11.4 | 45.9 |
| 3 | 1.4 | - | - | 1.4 | 0.1 | - |
| 4 | 8.0 | 4.9 | 0.4 | 4.4 | 1.9 | 0.2 |
| 5 | 5.7 | 3.4 | 2.5 | 8.7 | 3.5 | 1.5 |
| 6 | 18.2 | 13.7 | 7.0 | 26.2 | 14.9 | 6.5 |
| 7 | 0.5 | 0.6 | - | 0.7 | 0.9 | - |
| 8 | 8.0 | 1.9 | 0.1 | 12.8 | 3.6 | 0.2 |
| 9 | 0.4 | - | 1.1 | - | 0.2 | 1.0 |
| 0-4 | 67.3 | 80.4 | 88.2 | 51.5 | 76.9 | 90.7 |
| 5-9 | 32.7 | 19.6 | 11.8 | 48.5 | 23.1 | 9.3 |

* The Standard International Trade Classification system classifies all commodities under the following ten Sections:

0 - Food.
1 - Beverages and Tobacco.
2 - Crude Materials, inedible except Fuels.
3 - Mineral Fuels, lubricants and Releted Products.
4 - Animal and Vegetable Oils and Fats.
5 - Chemicals.
6 - Manufactured goods classified chiefly by material.
7 - Machinery and Transport Equipment.
8 - Miscellaneous manufactured articles.
9 - Miscellaneous Transactions and Commodities n.e.s.

This is shown in Table 2. From this table we can make three major observations on the commodity composition of East African exports to the three markets: (a) while in the trade with the Neighbours and the rest of the world East African exports are concentrated in SITC sections 0 and 2 i.e. food, and crude inedible materials excluding fuels, in inter-country trade exports are distributed over a large number of commodity sections - the most important being food, manufactured goods classified chiefly by material, tobacco and beverages, and miscellaneous manufactured goods, in that order. (b) If we take SITC section 0 - 4 to be primary products (which is true, although we should keep in mind that in section 0 there are some manufactured foods e.g. biscuits and that section 1 includes manufactured tobacco; while section 2 includes phyrethrum extract), and SITC sections 5-9 to be manufactured goods (again this is by and large true, although in section 6 base metals and diamonds are included), it will be noticed that manufactured goods play the greatest part in inter-country exports. For instance while manufactured goods accounted for 48.5% of total inter-country exports in 1963, the corresponding ratios in exports to the Neighbours and the rest of the world were only 23.1% and 9.3% respectively. Actually in the latter case this ratio would have been very small indeed if exports of diamonds, copper, and gold (worth slightly over £10.4 million in 1963) were excluded. In fact taking both the Neighbours and the rest of the world together we notice that if we exclude diamonds, copper and gold, exports of manufactured goods to these two markets were only a third of the value of manufactured inter-country exports -- or about £5 million compared with well over £15 mn. (c) It will also be noticed from table 2 that it has been in inter-country exports that substantial shifts in the relative importance of various SITC sections have taken place in the period 1959-63, with manufactured goods becoming increasingly more important. Manufactured goods for instance, have increased their relative share in total inter-country exports from 32.7% in 1959 to 48.5% in 1963, while in exports to the Neighbours (and these are countries at broadly the same stage of development as East Africa) the increase has been only from 19.6% to 23.1%; and in the case of exports to the rest of the world the percentage share of manufactured goods actually declined slightly in this period. It will also be noticed that whereas the percentage share of food exports in inter-country trade has declined between 1959 and 1963, in the case of exports to the other two markets it has actually increased.

The increasing importance of manufactured goods in inter-country trade reflects the process of import substitution that has been taking place in East Africa. This import substitution has been achieved under a framework of proctection -- by tariff rates of 25-$33\frac{1}{3}$%. Such domestically manufactured goods as cotton fabric piece-goods, shoes, steel doors and windows, aluminium and metal containers and utensils, bicycle tyres and tubes, etc. enjoy a good measure of protection. The same is also true of certain foodstuffs, and beverages and cigarettes. The fact that manufactured goods have become important in these exports only recently emphasises a point made earlier; namely that mere existence of a common market is of little effect in encouraging industrialisation <u>unless</u> the opportunities it offers are seized. The East African common market has been in existance for the last forty years; but it was only after World War II that inter-country trade began growing steadily and, as far as manufactured goods are concerned, it is only in the last few years that this trade has become important. The most rapid expansion in inter-country exports of manufactured goods has been in the last five years: and between 1959 and 1963 inter-country exports in SITC sections 5-9 more than doubled in value.

The extent of import substitution which has taken place can crudely be estimated by showing the value of inter-country imports and expressing this value as a proportion of East Africa's retained imports i.e. all imports from abroad minus re-exports. This method is crude because it does not take into account those goods produced and consumed in each East African country: but still as a crude method it helps to indicate where import substitution has been significant. In Table 3 East African inter-country imports (the same value as inter-country exports for East Africa as a whole) in various SITC sections are expressed as percentages of retained imports for 1959 and 1963.

TABLE 3

SITC DISTRIBUTION OF EAST AFRICAN RETAINED IMPORTS (A), AND INTER-COUNTRY IMPORTS (B): 1959 AND 1963

in £.000

| SITC Section | 1959 A | 1959 B | 1959 B% of A | | 1963 A | 1963 B | 1963 B% of A |
|---|---|---|---|---|---|---|---|
| 0 | 8,346 | 6,188 | 74.6 | 0 | 7,877 | 8,889 | 112.8 |
| 1 | 1,281 | 4,724 | 368.8 | 1 | 1,072 | 4,521 | 421.7 |
| 2 | 876 | 727 | a | 2 | 1,313 | 907 | 69.1 |
| 3 | 9,780 | 279 | 2.9 | 3 | 9,416 | 435 | 4.6 |
| 4 | 671 | 1,604 | 239.0 | 4 | 1,253 | 1,393 | 111.2 |
| 5 | 8,216 | 1,145 | 13.9 | 5 | 10,699 | 2,728 | 25.5 |
| 6 | 40,011 | 3,654 | 9.1 | 6 | 46,435 | 8,249 | 17.8 |
| 7 | 30,472 | 103 | 0.3 | 7 | 36,487 | 205 | 0.6 |
| 8 | 9,232 | 1,603 | 17.4 | 8 | 12,149 | 4,020 | 33.1 |
| 9 | 5,456 | 71 | 1.3 | 9 | 6,575 | 107 | 1.6 |
| TOTAL | 113,350 | 20,098 | 17.7 | TOTAL | 133,273 | 31,455 | 23.6 |

Source: Annual Trade Reports.

Note: a = For this section, retained imports were smaller than re-exports, thus giving a negative value. Such negative values result from the fact than not all goods re-exported to foreign countries are re-exported in the same year as they were imported. For this particular section, re-exports were £992,000 in 1959, compared with £876,000 worth of imports in that year.

In this table we need to observe that during the five-year period covered East Africa has carried a process of import substitution in practically all SITC sections. Adding all sections together we notice that while inter-country imports as a proportion of retained imports were 17.7% in 1959, by 1963 this ratio had risen to 23.6%. In particular we should observe that in the SITC sections which contain most manufactured products (i.e. sections 5,6 & 8) the ratio of inter-country imports to ratained imports has risen by more than the average rise. In these sections the rises have been: section 5 from 13.9% to 25.5%; section 6 from 9.1% to 17.8%; and section 8 from 17.4% to 33.1%. These increases are impressive because in 1963 retained imports were a good deal more in each of these sections than they were in 1959.

It should also be observed that while inter-country imports of food were smaller than retained imports in 1959, by 1963 they were greater than the latter by about £1 million. Retained imports of food have actually declined over the last five years, while inter-country imports of food have increased by £2.7 million, and we can expect this trend to continue, as it should because import substitution in food is often as important as import substitution in manufactured goods, especially where foreign imports of food are really manufactured products. An underdeveloped country should attempt to provide herself with food requirements -- so that foreign exchange is used primarily for importing capital goods which are needed for investment.

One rather interesting thing to notice from Table 3 is that not only has there been a fall in the value of retained imports of beverages and tobacco (SITC section 1), but the value of inter-country imports of these goods has also fallen. However, this fall in the value of inter-country imports of these goods should not be taken as indicating that East African production of these goods has fallen: on the contrary; there has been a remarkable increase in their production, but each country is now absorbing an increasing proportion of its production of these items. This is especially true in the case of beer.

In concluding this section we should emphasise again that the amount of industrialisation that has taken place in East Africa owes much to the larger market created by the existence of the common market. Taking East Africa as a whole, her population is more than $3\frac{1}{2}$ times that of Uganda, about three times that of Kenya, and about $2\frac{1}{2}$ times that of Tanganyika. Moreover, as far as the monetary gross domestic product is concerned, the East African total is 2.4 times that of Kenya, 3.3 times that of Tanganyika, and 3.6 times that of Uganda. Consequently East Africa as a whole offers a larger market than any of the three countries could offer, and can therefore support more and bigger industries.

## III

In section II we have attempted, albeit too briefly and inadequately, to indicate the effect of the common market on the industrialisation, through greater inter-country trade, of East Africa taken as a whole. In this section we shall discuss, again briefly, the effects of this common market on the development of each East African country.

In general, the extent to which a participating country benefits from a common market depends on whether it can substantially increase its exports to the other participants, and, in the case of an underdeveloped country aspiring to industralise, on the commodity composition of its exports. If a country in a common market or customs union just simply shifts its sources of imports from third countries to the partners and does not increase her exports to the latter, there is every likelihood that the country in question will lose in the operation of the common market -- if only because imports from partner countries are likely to be, initially at least, more expensive than those from third countries. Moreover, in the case of underdeveloped countries it is likely that industrialisation will tend to concentrate in given areas because of a whole lot of possible factors -- economies of scale, concentration of entrepreneurial ability in a given country, concentration of high incomes, better transportation facilities, etc. In fact it seems as if the "polarisation effect" of a common market

is initially stronger than the "trickling-down effect",[7] with the result that former disparities in growth rates and levels of income among member countries are likely to be intensified by the formation of the common market unless deliberate policy steps leading to planned intervention are taken to reduce the more powerful polarisation effect. The trickling-down process (or spread effect as Myrdal calls it) is initially less powerful because the factors which bring it about (increase in demand for the poorer members' goods; relocation of industries or attractiveness in industrial expansion because of wage differentials, lower rents, etc; and transmission of technical knowledge, skills, etc.) operate only after some considerable industrialisation has taken place. Indeed, in the early stages of development the poorer members are likely to lose even more because entrepreneurial ability and capital are likely to migrate to the more rapidly growing areas.

The points made above provide the basic framework for assessing the effects of the common market on each East African country. In Table 4a we show the value of each country's exports to, and imports from, the rest of East Africa during the period 1959 through 1963; and in Table 4b we have shown these same exports and imports as percentages of total East African inter-country exports and imports. Analysis has been confined to the last five years essentially for two reasons: (a) the published inter-country trade data up to 1958 inclusive include excise taxes levied on excisable commodities, and duties levied on dutiable imports used in production. Although it is possible to estimate and isolate excise taxes elements in the published data, it is virtually impossible to estimate and isolate elements of import duties included. (b) It is only in the last few years that inter-country has become significant: as recently as 1954 the total value of this trade was £12.5 million exclusive of excise taxes on sugar, beer, cigarettes and tobacco.

From Tables 4a & 4b we can make the following observations: (a) Kenya is the main supplier of goods in this trade: thus while her percentage share in total inter-country exports has averaged 62.6% over the last five years, Uganda's percentage share has averaged 27.1% and Tanganyika's share only 10.3%. A more dramatic way of showing Kenya's predominant position in these exports is to look at the real figures: in 1959 Kenya's exports were five times those of Tanganyika and two-and-half times those of Uganda; and in 1962 they were seven times those of Tanganyika but still two-and-half times those of Uganda. In fact Kenya has, over the last five years, tended to increase her percentage share in these exports, although in 1963 this share declined slightly -- largerly due to a sudden increase in the share of Tanganyika. (b) it will be seen that while Kenya's exports increased by 7.5 million between 1959 and 1963, Uganda's increased by £3 million, and Tanganyika's actually declined between 1959 and 1962 and only showed a significant increase in 1963. But it is still important to notice that even at this record level, Tanganyika's exports, as a proportion of total inter-country exports, were smaller than they were in 1959 -- by almost 2%.

7. This terminology has been employed by Hirschman (Strategy of Economic Development, Yale University, Press, 1958. pp 187-120). Polarisation Effect means that growth in economic activity (rise in incomes, employment, and industrialisation) is concentrated in certain areas; while Trickling-down Effect means the process of spreading industrialisation, high incomes and employment throughout the common market or customs union area.

Myrdal has a similar analysis, see G. Myrdal, Economic Theory and Underdeveloped Regions, London, 1957. Chapters 3-5.

TABLE 4a

INTER-COUNTRY EXPORTS & IMPORTS, 1959-1963

in £,000

| | KENYA | | UGANDA | | TANGANYIKA | |
|---|---|---|---|---|---|---|
| | Exports | Imports | Exports | Imports | Exports | Imports |
| 1959 | 12,297 | 5,488 | 5,228 | 6,510 | 2,574 | 8,100 |
| 1960 | 13,773 | 6,995 | 6,694 | 6,613 | 2,324 | 9,182 |
| 1961 | 15,948 | 6,995 | 6,856 | 7,437 | 2,234 | 10,605 |
| 1962 | 17,320 | 7,339 | 7,055 | 7,740 | 2,391 | 11,685 |
| 1963 | 19,790 | 9,163 | 8,243 | 9,933 | 3,423 | 12,358 |

TABLE 4b

COUNTRY PERCENTAGE SHARES IN INTER-COUNTRY EXPORTS AND IMPORTS, 1959-1963

EXPORTS

| | 1959 | 1960 | 1961 | 1962 | 1963 |
|---|---|---|---|---|---|
| Kenya | 61.2 | 60.4 | 63.7 | 64.7 | 62.9 |
| Uganda | 26.0 | 29.4 | 27.4 | 26.4 | 26.2 |
| Tanganyika | 12.8 | 10.2 | 8.9 | 8.9 | 10.9 |

IMPORTS

| | 1959 | 1960 | 1961 | 1962 | 1963 |
|---|---|---|---|---|---|
| Kenya | 27.3 | 30.7 | 27.9 | 27.4 | 29.1 |
| Uganda | 32.4 | 29.0 | 29.7 | 28.9 | 31.6 |
| Tanganyia | 40.3 | 40.3 | 42.4 | 43.7 | 39.3 |

Sources: Annual Trade Reports.

Looking at imports the picture is reversed: the main importer is Tanganyika, followed by Uganda and then Kenya. Moreover, in the period 1959-62 Tanganyika actually increased her percentage share in these imports -- from 40.3% in 1959 to 43.7% in 1962 -- while Kenya's share remained the same and Uganda's declined but recovered in 1963. In 1963, however, Tanganyika's share in these imports dropped suddenly, mainly because she increased her inter-country exports.

What needs emphasising very strongly (and this is something not brought out in the figures provided in the tables) is that the small shares of Uganda and Tanganyika in this trade arise from the fact that they hardly trade between themselves, while each of them tends to trade primarily with Kenya. For instance in 1963 85.2% of Tanganyika's inter-country exports went to Kenya and in the case of Uganda the corresponding ratio was 75.8%. It therefore seems most unlikely that these two countries could substantially increase their shares in this trade without

trade without increasing trade between themselves.[8]

Summing up our discussion so far, the general picture is that Kenya is, by a large margin, the main exporter in inter-country trade while Tanganyika is the main importer, with Uganda somewhere between but nearer Kenya's position. We can therefore say that, just looking at the total volume of inter-country trade, Kenya has gained the most in the common market, that Uganda has also gained, and that Tanganyika has certainly gained the least and has probably lost. This conclusion is reinforced by examination of the commodity composition of each country's inter-country exports and imports which is indicated in Table 6 below.

TABLE 6A

COMMODITY COMPOSITION OF EACH COUNTRY'S INTER-COUNTRY EXPORTS, % DISTRIBUTION BY SITC SECTIONS: 1959 & 1963

| | 1959 | | | 1963 | | |
|---|---|---|---|---|---|---|
| | KENYA | UGANDA | TANGANYIKA | KENYA | UGANDA | TANGANYIKA |
| 0 | 33.4 | 19.5 | 41.1 | 24.8 | 33.2 | 36.4 |
| 1 | 19.9 | 36.6 | 14.2 | 15.1 | 17.2 | 3.1 |
| 2 | 1.4 | 1.6 | 18.3 | 0.9 | 1.6 | 17.2 |
| 3 | 0.2 | 3.8 | 2.5 | 0.3 | 4.2 | 1.1 |
| 4. | 1.6 | 20.3 | 13.4 | 1.0 | 10.9 | 8.4 |
| 5 | 7.1 | 3.3 | 3.9 | 11.9 | 4.0 | 1.5 |
| 6 | 22.8 | 13.9 | 4.9 | 27.3 | 27.7 | 16.5 |
| 7 | 0.8 | 0.1 | 0.1 | 0.9 | 0.3 | 0.2 |
| 8 | 12.3 | 1.0 | 1.4 | 17.3 | 0.8 | 15.4 |
| 9 | 0.5 | - | 0.1 | 0.5 | 0.1 | 0.2 |
| 0-4 | 56.5 | 81.7 | 89.6 | 42.1 | 67.1 | 66.2 |
| 5-9 | 43.5 | 18.3 | 10.4 | 57.9 | 32.9 | 33.8 |

TABLE 6B

COMMODITY COMPOSITION OF EACH COUNTRY'S INTER-COUNTRY IMPORTS % DISTRIBUTION BY SITC SECTIONS: 1959 & 1963

| | 1959 | | | 1963 | | |
|---|---|---|---|---|---|---|
| | KENYA | UGANDA | TANGANYIKA | KENYA | UGANDA | TANGANYIKA |
| 0 | 25.1 | 37.7 | 29.1 | 38.2 | 24.0 | 24.3 |
| 1 | 25.9 | 19.2 | 25.4 | 11.7 | 13.1 | 17.4 |
| 2 | 9.3 | 1.9 | 1.1 | 7.3 | 1.3 | 0.9 |
| 3 | 4.7 | 0.2 | - | 4.2 | 0.2 | 0.2 |
| 4 | 19.9 | 3.1 | 3.8 | 10.4 | 1.9 | 2.0 |
| 5 | 2.9 | 7.1 | 6.5 | 2.8 | 12.9 | 9.6 |
| 6 | 11.0 | 20.0 | 21.6 | 19.2 | 29.9 | 28.5 |
| 7 | 0.1 | 0.7 | 0.7 | 0.2 | 1.0 | 0.8 |
| 8 | 1.1 | 9.9 | 11.1 | 5.9 | 15.5 | 15.7 |
| 9 | 0.1 | 0.2 | 0.6 | 0.1 | 0.3 | 0.5 |
| 0-4 | 84.8 | 62.1 | 59.5 | 71.8 | 40.4 | 44.9 |
| 5-9 | 15.2 | 37.9 | 40.5 | 28.2 | 59.6 | 55.1 |

8. Two reasons why trade between Uganda and Tanganyika is small and has tended to stagnate easily come to mind: (i) the fact that transportation facilities between the two countries are very poor indeed, while each of these countries has effective communication and transportation links with Kenya. (ii) Also important is the fact that Kenya is the more developed partner, and has therefore more to sell to the rest of East Africa, and in some cases buy raw materials e.g. unmanufactured tobacco.

From table 6 it will be observed that Kenya's exports to the other two countries consist mainly of manufactured goods (with this trend pointing strongly upwards), while her imports consist mainly of primary products. On the other hand Tanganyika's exports are mainly primary products, although from 1959 to 1963 the share of manufactured goods in her exports increased from 10.4% to 33.8%. However, these percentages are misleading unless they are seen in the background of the real values involved. Looking at the real values of all inter-country exports and imports of manufactured goods, in 1963 Tanganyika's percentage shares in the former and the latter were 7.6% and 44.4% respectively, while Uganda's shares were 17.7% and 38.7%, and Kenya's shares 74.7% and 16.9%, again respectively.

It is therefore true to say that the common market has encouraged industrialisation most in Kenya, and it is likely that it has held back setting up manufacturing industries in Tanganyika, although certainly not in Uganda. The word likely is most important, for it would be wrong to suppose that but for the existence of the common market Tanganyika would now be having a large and flourishing manufacturing sector. It is true that the availability of a protected market has been of crucial importance in the emergence and expansion of some manufacturing activities in Kenya (for almost all Kenya's exports of manufactured goods are sold to the rest of East Africa); but other factors have also been important. For instance it is not always realised that nearly 50% of the total East African monetary income is in Kenya, and that Kenya actually consumes large proportions of the manufactured goods which she produces. In other words, the domestic market of Kenya has been of considerable importance in the minor industrialisation which has taken place in that country. There are other factors too e.g. the concentration of Europeans and Asians in Kenya's main towns (and it is these two communities which have supplied most of the entrepreneurial ability in East Africa); the more favourable geographical position of Kenya; and the fact that economically at least the British colonial policy tended to favour Kenya. Moreover, as far as the growth of each country's monetary gross domestic product is concerned, it should not be forgotten that after the Korean War commodity boom collapsed, all three countries were hit hard, -- because they depend heavily on exports of a few primary commodities for their monetary incomes. But this dependence is greater in both Uganda and Tanganyika -- and greater in Tanganyika than in Uganda -- and the latter countries were therefore hit harder than Kenya by the collapse of the Korean War commodity boom.

However, this paper does not deny that the more stable and higher rate of economic growth in Kenya[9] over the last six or so years owes a lot to the very rapid increase in her exports to both Uganda and Tanganyika. For instance if between 1954 and 1963 Tanganyika's inter-country exports had increased by the same amount as the increase in Kenya's inter-country exports, her monetary GDP, other things being equal, would have been £22 million greater in 1963.[10] Of course this is not to suggest that either Uganda or Tanganyika would have done much better but for the common market: what we can say for certain is that these two countries would have done better had their inter-country exports increased by more than they did.

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9. Between 1954 and 1961 Kenya's monetary GDP increased by £64.3 mn, while Uganda's increased by £18.9 million, and Tanganyika's by £35.1 mn. However, due to greater earnings of domestic exports in 1963, Uganda's monetary G.D.P increased from £107.9 million in 1962 to £128.7 million in 1963, and Tanganyika's increased from £123.3 mn to £140.3 mn; while, Kenya's increased from £180.9 mn to only £193.3 mn. This is an additional fact to emphasise that had both Uganda and Tanganyika kept up a reasonable rate of growth in the value of their domestic exports during the '50s, their monetary GDP would not have increased by so much less than Kenya's.

10. This estimate is based on some regression analysis contained in my forthcoming monograph.

IV

Measures to improve the operation of the Common Market.

The history of the common market has not been a peaceful one: and there have been two major controversies. The first controversy was in 1920s when, after the Congo Basin (Open Door Treaty) countries (of which East Africa was a member) were allowed to raise their tariffs above the 10% ceiling fixed by the Brussels Conference of 1890, Kenya advocated for and achieved introduction of protective tariffs in East Africa. The first tariffs covered timber, sugar, wheat and wheat-flour, butter, ghee, cheese, ham and bacon. After these tariffs were in existence for a few years Uganda, and Tanganyika less energetically, attacked this policy, mainly on grounds of welfare[11] -- that Kenya goods were of poor quality, high-priced, and that the protected industries had not proved that they could stand on their own even after a period of considerable protection. It was also claimed that Kenya's production of these goods could not satisfy the East African demand. However, after a reduction (not elimination) of these tariffs in 1930, the controversy ebbed, helped by the Great Depression which undermined faith in free trade and laisses-faire policies even in Uganda.

The second controversy and which is still with us started after the collapse of the Korean War commodity boom. In this controversy we can distinguish three arguments: (a) loss of economic sovereignty; (b) loss of revenue; and (c) unequal growth rates and industrialisation among the three countries. We can quickly dispose of the first argument: in any common market or customs union where there is free movement of goods and factors of production, each country's ability to follow an entirely independent line in its economic policies is reduced to a greater or less extent -- depending on its economic importance in the common market as a whole. This loss of sovereignty is especially serious where economic co-operation is limited only to tariff policy, with no co-ordination in other development policies. In Uganda it has been claimed that her membership in the common market puts her into a 'fiscal strait - jacket' -- which is true to an extent. However, without going into great detail about this, we can say that unless in a common market there is co-ordination and harmonisation of economic policies (and social policies in most cases) the danger of such economic integration breaking up is great. This solidly applies to the East African common market.

The loss of revenue argument.

Allocation of revenue is always a thorny problem in a customs union where member countries depend heavily on customs duties for their revenue -- as the East African countries do. It is argued that by importing Kenya goods (because Uganda and Tanganyika have not expanded their inter-country exports as much as Kenya has done -- as we saw earlier) instead of foreign ones, Uganda and Tanganyika lose revenue in the process, while Kenya maintains her revenue through proceeds from income tax levied on income derived from import substitution activities.

11. For Uganda's arguments in this controversy see Uganda Government, Report of the Tariff Committee, November, 1929. Entebbe, Uganda did, however, recognise the importance of maintaining the customs union, and pointed out that considerable effort should be made to "ensure that there shall be a customs union in fact as well as in name".

For Kenya's arguments, see Kenya Government, Report of the Tariff Committee, May 1929. Nairobi.

This argument has some substance, but it has been enormously exaggerated. A crude method of estimating each country's loss of revenue is to take her exports to the rest of East Africa and multiply these by the appropriate rate of duty had the rest of East Africa imported these goods from foreign countries (call this A); then do the same for the imports of the country in question from the rest of East Africa (call this B); and then substract A from B. This method is not satisfactory because it rests on the assumption that income levels, patterns and levels of consumption in each country would have been the same had there been no common market. This would be a very brave assumption. However, it was attempted - a most laborious job for the calculation had to be done for each dutiable commodity. Unfortunately, it was not found easy to deal with excisable commodities -- for two reasons: (i) excise taxes change frequently and, in the case of cigarettes (the chief commodity in the excisable goods), excise tax rates are given by specifications which are not published in the available trade data; (ii) in most cases excise taxes are much lower than external tariff: for instance in the case of cigarettes the average excise tax for 1962 works out to be about Shs.15 per pound, while the external tariff is Shs.44 per pound i.e. a difference of Shs.29 per pound. If then a calculation was made for cigarettes, Tanganyika would have appeared to have lost more than £4.4 million in 1962. Even after subtracting excise tax revenue on cigarettes which Tanganyika received from these imports (excise tax revenue is given to the consuming country) Tanganyika would still appear to have lost more than £3 million. It was felt therefore that our assumption that consumption levels would have been the same was so unrealististic in the case of excisable commodities that we decided not to include SITC section 1 (this section includes most of the excisable goods) in our final estimates. This is reasonable, because in the case of cigarettes for instance an application of full external duty would have more than doubled the price of various brands of cigarettes, and it would be most unrealistic to expect that consumption of cigarettes would have been the same even at these high prices.

When the calculation on dutiable non-excisable commodities was carried out for 1962, it was found that Tanganyika's loss of revenue was £1.366 million, and Uganda's loss £664.000. These figures are smaller than one would infer from the volume and intensity of the controversy centred on this point: it is not often realised that some of these two countries' inter-country exports to Kenya e.g. onions and non-leather shoes from Tanganyika and cotton fabric piecegoods from Uganda, carry high rates of duty if imported from abroad.

The problem of loss of revenue to these two countries is now being solved to an extent by the use of the Raisman Formula,[12] but this should be regarded as a temporary device, if only because it stresses the revenue problem instead of the more fundamental development problem of each country. This brings us to the third argument -- unequal growth rates.

Unequal Growth Rates.

It has already been indicated that Kenya has been industrialising faster than eigher Uganda or Tanganyika. It has also been emphasised that Kenya's more rapid growth owes its existence to other factors, besides the common market. However, it has become clear that the present differences are politically unaccept-able and that unless the other two countries are somehow give-

12. See Report of the Economic and Fiscal Commission, H.M.S.O. Cmnd. 1279. February, 1961.

the opportunity to set up industries, the common market is in great danger of breaking up. Where there are unequal growth rates among members of a common market and where it is felt that the common market is increasing the existing disparities, there are three courses of action which can be taken: (i) a complete break-up of the common market; (ii) a dilution of the common market; or (iii) closer economic integration. In East Africa, if a complete break-up occurs it is certain that each country would lose, and it is not improbable that Tanganyika and Uganda would lose more in the long-run even if it might appear that there are some short-run benefits. Moreover, we also need to point out that if the common market breaks up it is exceedingly unlikely that the common services now being run by EACSO would continue to be operated jointly for very long, and this would be a very serious loss, especially to both Uganda and Tanganyika. Therefore, if rapid growth rates are to be achieved in each country, considerable effort and sacrifice should be made to avoid a break-up of the existing economic integration.

The above conclusion leaves us with alternatives (ii) and (iii). To start with the dilution of the common market: because of the existence of the common market, aided by the existence of a common currency and close physical proximity, each country is now unable to use in full some of the instruments, usually available to a single country, for its industrialisation programme. Such instruments include company taxation, monetary policy, and tariff policy. These are now more or less uniform in East Africa, and it is possible that perhaps Uganda and Tanganyika could benefit, even if only slightly, if they followed policies likely to make them more attractive than Kenya -- as long as Kenya did not retaliate, a most unlikely assumption. Moreover, the possibility of attracting large-scale industries into Uganda and Tanganyika without giving these industries access to the Kenya market should be heavily discounted. We are therefore left with the last alternative i.e. closer economic integration which would, paradoxically, allow some kind of dilution of the common market to take place in favour of Uganda and Tanganyika without breaking up the common market altogether.

The fact that the present strains and tensions in the common market call for, if each country is to benefit in the long-run, closer economic integration rests on the fact that such closer integration would allow co-ordinated economic policies and planned intervention to be introduced in favour of those areas lagging behind. The truth is that most of the present tensions and strains in the common market arise from the fact that although there is a common market there is not as yet a <u>common economic policy</u>. A common economic policy should have, as one of its main objectives, planned distribution (through various possible devices) of industry throughout East Africa. Strong emphasis should be laid on the word <u>distribution</u>, not redistribution; for even Kenya is not really an industrialised country and there are very few (if any) industries which can be redistributed. In other words the policy adopted should be dynamic, rather than static, and should be designed to distribute industries within a framework of general economic expansion in this whole area. The possibility of success if such a policy were adopted is great; for the scope of further import substitution on an East African basis is very great in relation to the amount achieved so far. Just looking at some goods which East Africa produces but not in enough quantities so that she still has to import from abroad in order to meet domestic demand for them, we get the following:

EAST AFRICAN SELECTED IMPORTS, 1963: in £,000

| Item | £,000 |
|---|---|
| Tinned milk and cream | 1,385 |
| Rice | 608 |
| Manufactured tobacco, incl. cigarettes and cigars. | 177 |
| Matches | 257 |
| Chemicals, organic and inorganic | 1,179 |
| Disinfectants, insecticides, etc. | 1,288 |
| Manufactured fertilisers | 1,281 |
| Footwear | 553 |
| Clothing | 3,997 |
| Blankets and travelling rags. | 1,517 |
| Cotton fabrics | 8,608 |
| Corrugated iron sheets | 418 |
| Other iron sheets, plates, hoops, strips, etc. | 3,585 |
| Paper and paperboard manufactures | 4,090 |
| Wood and cork manufactures | 517 |
| Rubber tyres and tubes | 2,864 |
| Soap and cleansing preparations | 672 |
| Paints and varnishes | 884 |
| TOTAL | 33,881 |

Source: Annual Trade Report of Kenya, Uganda and Tanganyika, 1963.

The important thing to realise is that East Africa produces all these goods, but not in adequate quantities to satisfy domestic demand. Incidentally, most of them are consumer-goods, and some of them require relatively simple technology and are therefore capable of being replaced by domestic products. It is unwise to treat industrialisation as the existence of such spectacular plants as iron and steel factories: for industrialisation has to start with simple manufactures and as import substitution succeeds the foreign exchange saved can be used to import more capital goods for extending further the process of import. substitution. Moreover, as manufacturing activities increase the country becomes more prepared and able to engage in production of more sophisticated goods. More relevant to our discussion, however, is the fact that it is only through greater import substitution that Uganda and Tanganyika can raise their percentage shares in inter-country exports, especially those of manufactured goods. But also important is the fact that the best way to increase the volume of import substitution is to tackle it on an East African basis. This seems to have been recently recognised by the three governments; and at a meeting of ministers of finance, and of commerce and industry held in Kampala last April, future industrialisation was discussed. This resulted in each country being allocated exclusive rights to establish certain specific industries: Tanganyika was allocated motor-tyre manufactures, truck assembly, and radio manufacture; Uganda was allocated two -- nitrogenous fertilisers, and bicycle manufacture; and Kenya was allocated one -- light bulb

manufacture. If such planned import substitution on an East African basis could be increased, the three countries would mutually gain, besides, of course, leading to less tension in the common market.

The Kampala Agreement went further than merely allocating industries to each country: it was also agreed that in order to reduce the present imbalance in inter-country trade (i.e. in order to increase the share of Tanganyika, and to a lesser extent Uganda, in inter-country exports) two further actions could be taken: (a) for a number of industries such as beer, footwear, and cigarettes which are to be found in each country, the companies involved should be approached and persuaded that each country's needs of these goods should be produced locally; (b) in order to hasten the removal of imbalance in inter-country trade, it was also agreed that where a country wants to produce locally or increase production of some goods which it is currently importing from the rest of East Africa, quotas could be applied against the rest of East Africa as long as the industries concerned could be operated efficiently in the country in question. Several observations on this quota system are in order: (i) the system would benefit East Africa as a whole only if quotas were applied in those cases where the country had immediate and adequate capacity to produce the goods in question. If quotas exceeded this capacity and imports from the rest of East Africa were replaced by foreign imports (and a country might attempt to do this because of additional revenue from customs duties on foreign imports), the common market itself would be in great danger of breaking up. (ii) quotas should be made temporary. One of the benefits accruing from the common market is that through competition efficiency and increases in productivity are encouraged, and if quotas were permanent they would insulate inefficient industries against such competition. Moreover, although some industries could be operated efficiently in each country's domestic market, it is likely that additional benefits could be secured if there was country specialisation in some of these industries. (iii) It would be wrong to think that having each country's inter-country trade in complete balance would benefit the area as a whole or even the country in question in the long-run. Even in a single country it is impossible to have simultaneous and equal growth rates in all its regions and sectors: there will be those areas and industries which will grow faster than the rest. Therefore the word balance needs very careful definition -- since complete balance can now be achieved only by impoverishing some of the members, and it is to be questioned whether this would be to any country's long-run interests. The main danger in the quota system is that their introduction in one country is likely to be followed by their introduction in the rest of East Africa, unless these quotas are clearly defined, and are instituted only after complete agreement and within a very strong framework of economic co-operation.

The Kampala Agreement therefore offers possibilities of maintaining and improving the common market so that each participating country can benefit. But we have seen that it has its own dangers which should not be ignored. Moreover, we have to keep in mind the fact that attempts to redirect foreign capital from one East African country to another are likely to appear uncalled for and premature to foreign entrepreneurs, and it is therefore likely that strict attempts to redirect foreign capital could reduce its inflow -- for afterall East Africa has to compete with many other countries for this very scarce factor. Therefore planned distribution of industry has to rely more, at this stage at any rate, on those resources actually available to these countries, although this is not to deny that foreign capital could not be persuaded to go to certain areas through special inducements. These two points emphasise the importance of co-ordinated economic planning.

4th December, 1964.